No. 3994

IN THE

United States Circuit Court of Appeals

For the Ninth Circuit

H. ALLEN RISPIN,
Plaintiff in Error,

vs.

THE MIDNIGHT OIL COMPANY
(a corporation),
Defendant in Error.

BRIEF FOR DEFENDANT IN ERROR.

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As viewed by defendant in error the principal point of law presented in the opening brief of plaintiff in error is whether material issues were made by those allegations in the answer which are in substance, as follows:

FIRST. That the contract in suit was not such that it was impracticable or extremely difficult to fix the actual damage occasioned by a breach on the part of plaintiff in error.

SECOND. That defendant in error suffered no actual damage by the failure to drill the well as

agreed, as the property in question was barren of oil.

Defendant in error contends that the allegation in the complaint that it was impracticable and extremely difficult to fix the damage is mere surplusage, as this fact otherwise appears from the complaint. The complaint sets out the contract in full. It is an ordinary oil-well drilling contract providing for liquidated damages in case of breach. The courts are almost unanimous in holding that such contracts show upon their face that it is impracticable and extremely difficult to fix the actual damage.

In the case of *McComber v. Kellberman,* 162 Cal. 747, the action was for a breach of an oil-well drilling contract providing for certain payments for failure to drill the well within the time agreed. Defendant contended that plaintiff could not recover liquidated damages, because,

> "It was neither alleged or proven that the nature of the case is such that it would be extremely difficult or impracticable to fix the damages."

On this point the court said:

> "But if it were considered as liquidated damages the complaint and proof are sufficient to support the judgment. The nature of the case and the extreme difficulty of fixing damages arising from a breach of such a contract are fully shown by the lease itself."

This point was directly decided in *Escondido Oil Company v. Glasier,* 144 Cal. 500, in which case a general demurrer was sustained to the complaint which was based upon an oil-well drilling contract providing for liquidated damages in case of breach. The complaint merely set forth the substance of the contract between the parties, there being no allegation as to the difficulty of fixing actual damages. The court said:

> "However, as the case may be hereafter tried on its merits it is proper to say that in our opinion the agreement for liquidated damages should be upheld. The complaint sufficiently states the character and subject matter of the contract—'the nature of the case', to use the language of Section 1671 to show that upon its breach 'it would be impracticable or extremely difficult to fix the actual damages'. Fixing the amount of damages sustained in contracts for digging oil wells very similar to the one here involved was upheld in Gibson v. Oliver, 158 Pa. St. 277 and the cases there cited and it would seem that damages for breaches of contracts touching future interest in oil-wells of unknown value are of such *remote and speculative character* as to bring them peculiarly within the rule that the parties should have the right to fix them by mutual agreement. In the case at bar the right of plaintiff under the contract with the Insurance Company to test the land and to acquire a valuable interest therein, if the test proved successful, was limited in time and that right might be lost by failure of defendant to comply with his contract; and it was quite apparent that in such event it would be entirely impracticable to show

> plaintiff's loss or what otherwise would have been his gain."

This court cited the *Escondido Oil Company* case supra with approval in the case of *Blodgett v. Columbia Live Stock Company,* 164 Fed. 305, Judge Ross writing the opinion. In the Blodgett case an oil-well drilling contract providing for liquidated damages was being considered. The complaint set forth the contract and alleged that plaintiff had been damaged in the amount agreed upon as liquidated damages. The trial court gave judgment for the amount specified in the contract as liquidated damages, although no damages had been proved and although there was no allegation in the complaint that it was impracticable or extremely difficult to fix the amount of actual damage. A portion of the opinion of Judge Ross is as follows:

> "We think the judgment right. In the very nature of the case the damage which would result to the lessor by a breach of the lease by the lessee would *necessarily be indefinite, uncertain and speculative.* It was therefore eminently proper that the parties should fix such damages by mutual agreement."

Plaintiff in error cites the case of *Dyer v. Central Iron Works,* 182 Cal. 588, as authority for his contention. In said case on page 953 the court said:

> "A provision in a contract which fixes the amount of the damage in advance of a breach is void unless the party seeking to recover the sum agreed upon shows by pleading and proof

> that the provision is within the single exception to the general rule. (Long Beach City School District v. Dodge, 135 Cal. 401. Los Angeles Association v. Pacific Surety Company, 124 Cal. App. 95.) The complaint in the case at bar after enumerating the circumstances wherein the plaintiff sustained loss occasioned by defendant's breach alleges: 'That at all times it was and is impracticable and extremely difficult to fix the amount of damage for loss to plaintiff, or to prove the same.' This allegation which, of course is admitted by the demurrer, renders the complaint sufficient for the purpose of bringing the case within the exception provided by Section 1671 of the Civil Code."

Note that the court does not hold that this complaint would not have been sufficient if said allegation did not appear therein. In fact the court very properly might have held that such allegation was unnecessary as *the nature of the case* appeared from the contract set forth in the complaint and its nature was such as to bring it within the exception provided in Section 1671 of the Civil Code. On this point the court on page 593 states:

> "That *looking to the entire agreement, its scope, purpose and subject matter* and considering the result of the breach and the reasonableness of the sums agreed to be paid, it is clear there was an intent to estimate a just compensation for the loss sustainable in the event of a failure to comply with the agreement."

So in the case at bar, it likewise should be said:

> "That looking to the entire agreement, its scope, purpose and subject matter and considering the result of a breach and the reasonableness of the sums agreed to be paid, it is clear that there was an intent to estimate a just compensation for the loss sustainable in the event of a failure to comply with the agreement."

In fact this very court in the case of *Blodgett v. Columbia Live Stock Company,* supra, cited above, has said that an oil-well drilling contract similar in all essentials to the one in review here shows upon its face that the damages resulting from a breach

> "would necessarily be indefinite, uncertain and speculative. It was therefore eminently proper that the parties should fix said damages by mutual agreement."

and in effect held that in such a case it is unnecessary to allege facts already appearing from the contract itself.

In the *Dyer Bros. Iron Works* case, supra, the court, as appears from the extract of its opinion above quoted, cited *Long Beach School District v. Dodge,* 135 Cal. 401 and *Los Angeles Association v. Pacific Surety Co.,* 24 Cal. App. 95. In the *Long Beach District* case the contract sued upon was for the erection of a High School building within a certain time wherein it was provided that the contractor pay ten ($10) dollars a day as liquidated damages for every day that the said building remained incomplete

after the first day of February, 1898. Plaintiff offered evidence to prove that it was impracticable to fix the amount of actual damage, which evidence was admitted over defendant's objection. The court held that the said evidence was inadmissible as there was no averment in the complaint bringing the case within the exception provided for in Section 1671 of the Civil Code, as it did not appear from the contract that it would be impracticable or extremely difficult to fix the actual damage. The court said on page 404:

> "As an illustration that such evidence is necessary suppose the High School, during this period, occupied a leased building equally as well adapted to the purposes of the school as the one contracted to be erected, the damage sustained by the district would obviously be the rent of the building, and in such case stipulated damages could not control. It is clearly incumbent upon the party seeking to recover upon such agreement to show by averment and proof that his case is within the exception. Certainly the stipulation in the bond does not of itself, in the absence of all other evidence upon the subject, make it clear that it would be extremely difficult or impracticable to fix the actual damages that would result from the breach of the bond in not finishing the building by a certain day."

Again in the case of *Los Angeles Association v. Pacific S. Company,* the complaint was based upon an agreement to pay one thousand dollars as liquidated damages in case of failure to furnish capable

Japanese labor for picking and harvesting plaintiff's olive crop. The court, speaking of the evidence said:

> "It may or may not show the contract which Tajari is alleged to have abandoned was one, the nature of which rendered it impossible to fix the actual damages."

In other words this court held that the nature of the contract was such that it did not show in itself that it was impracticable and extremely difficult to fix actual damages.

The two cases last above referred to plainly are not cases in which the contracts in question show upon their face that it would be impracticable or extremely difficult to fix the actual damage sustained in case of breach. In such cases it may be that it must be alleged that it was impracticable and extremely difficult to fix the actual damages. But such cases are much different from the one at bar in which the contract itself shows that the nature of the case is such that it would be impracticable to fix the actual damages.

It is to be noted that in the case at bar it appears from the contract set forth in the complaint that defendant in error in consideration of the signing of the contract by plaintiff in error dismissed a suit which it had pending against plaintiff in error. What would have been the outcome of this suit? Defendant in error may have recovered judgment therein. This possibility defendant in error waived

as an inducement to plaintiff in error to agree that the Associated Oil Company would drill the well in question. The uncertainty of the outcome of said litigation is an added feature showing that it was impracticable or extremely difficult to fix the damages suffered by defendant in error in case plaintiff in error did not perform his contract.

Second: In cases involving contracts, such as oil-well drilling contracts, where it is proper for the parties to agree upon liquidated damages, actual damages are not an issue. In the case of *Wood v. Niagara Falls Paper Company,* 121 Fed. 818, this point was squarely presented and decided. The contract in suit related to the purchase and installation of certain machinery and provided that one hundred dollars per day was to be paid as liquidated damages for delay. The court held that such stipulated damages could not be construed as a penalty and that the plaintiff could not defeat or reduce recovery by showing that defendant sustained no actual loss by delay. The trial court excluded all evidence designed to show that no damages were suffered. This ruling was upheld by the appellate court, a portion of its opinion being as follows:

> "It is urged however that when it is made to appear in an action for a breach of contract that no actual damages have arisen, notwithstanding that the parties have agreed upon liquidated damages, the party in default is entitled to be relieved. That proposition is not sustained by weight of authority. On the con-

> trary according to the authority which is controlling upon this court the law is that the naming of a stipulated sum in such a contract to be paid for the non-performance of the contract is conclusive upon the parties in the absence of fraud or mutual mistake and evidence aliunde in respect to damages actually arising from a breach can not be received. Courts lean against forfeitures and toward construing such stipulations as penalties instead of liquidated damages when the amount on the face of the contract is out of all proportion to the *possible loss.* The question of this proportion has been simply an element entering into the consideration of the question of what was the intent of the parties, whether bona fide to fix damages or to stipulate an arbitrary sum as a penalty by way of security."

The case of *Wood v. Niagara Falls Paper Company* was reviewed and approved in the case of *Bosch Magneto Company v. Rushmore,* 255 Fed. 465. In the case of *Gibson v. Oliver,* 27 Atl. Rep. 961 (Pa.), the complaint was based upon an oil-well drilling contract providing for liquidated damages. In his answer defendant claimed that plaintiff was not entitled to the stipulated damages because wells drilled in the vicinity after the contract in suit was executed showed that there was no oil on the premises in question. The court held that this was no defense. The same defense was presented in the case of *Springer v. Citizens Gas Company,* 22 Atl. Rep. 986 (Pa.), and held insufficient by the court. It is to be noted that the case of *Gibson v. Oliver,* supra was cited with aproval by the California Su-

preme Court in the case of *Escondido Oil Company v. Glasier,* supra.

The authorities on the question whether actual damages are in issue where the parties have agreed upon liquidated damages are collected in a note to paragraph 264, 17 Corpus Juris, page 965. Paragraph 264 reads as follows:

> "Necessity of actual damages. The generally accepted rule is that proof of actual damage is unnecessary in order to recover a sum as liquidated damages. There are however some authorities that hold that proof of merely nominal damages will not support such a recovery and the view has also been taken that where the Court can see where no damages have been sustained, or there is no proof of damage, the provision for liquidated damages will not be enforced. However this would seem to be a statement in another form of the rule that the Court will not deem it to have been the intention of the parties to provide for liquidated damages where the sum reserved is grossly disproportionate to the damages sustained."

The cases cited in Corpus Juris as authority for the minority rule referred to in the above quotation are really not in point. For example: The leading case cited is *The Columbia,* 197 Fed. 661, in which the court reviewed a contract providing for the payment of demurrage. The court said:

> "My construction of the contract is that the libelant would pay damages as compensation for any loss the ship might suffer by the delay in completing the work on her. I find no evi-

> dence to show that she suffered any pecuniary loss."

In other words the court construed the contract to mean an agreement to pay the *actual amount* of damages suffered by delay in completing repairs on the ship. The basis of the court's construction of the contract was the meaning of the word "demurrage".

In any event the Supreme Court of the United States in the case of *Sun Publishing Company v. Moore,* 163 U. S. 682, upholds the principle that the question of actual damages is not pertinent in a case where the parties have properly agreed upon liquidated damages. In the Sun Publishing case the authorities are extensively reviewed and such cases as *Gay Manufacturing Company v. Camp,* 65 Fed. 794, cited by plaintiff in error, repudiated. This repudiation is in effect a repudiation of *Northwestern Fixture Company v. Kilborne,* 128 Fed. 256, cited by plaintiff on page 19 of his opening brief as authority for the proposition.

> "That a provision even for liquidated damages will not be enforced where no damages whatever have been sustained."

In the *Kilborne* case, supra, the contract in question was not an oil-well drilling contract, but an agreement by the defendant to sell sufficient of its stock in trade to pay off creditors and to turn the balance over to plaintiff in exchange for a portion of

plaintiff's capital stock. Defendant agreed to pay ten thousand dollars as liquidated damages for any default on its part. The court construed this contract to provide for a penalty and not liquidated damages. It therefore is not authority for the proposition that when a contract rightfully provides for liquidated damages evidence that no actual damages were sustained is admissible.

Plaintiff in error contends that the provision in the contract in suit for the payment of ten thousand dollars as liquidated damages is in fact a provision for the payment of a penalty. We submit that this contention is fully answered by the cases above cited by defendant in error. It is apparent that the contract does not contain a number of separate covenants of varying degree of importance, for the breach of any of which the stipulated sum of ten thousand dollars was to be paid. The object of the contract is single and its provisions all relate to that single object, namely, the drilling of the oil well within the time agreed. A similar contract was upheld as properly providing for liquidated damages and not a penalty in *Escondido Oil Company v. Glasier,* supra, and the other cases above cited.

The contention that the obligation of plaintiff in error to pay the stipulated sum of ten thousand dollars is collateral to another agreement and therefore must be construed as a penalty is not tenable. Plaintiff in error does not point out what the other agreement is to which the provision for liquidated

damages is collateral. The object of the contract in suit was to get the oil well drilled in the manner and within the time agreed. Surely it can not be successfully contended that the agreement to pay ten thousand dollars as liquidated damages was collateral to such object. If it be held that it is collateral to such object then the fact that it is collateral would seem to offer no objection, for the courts show no hesitancy in upholding similar agreements, as shown by the authorities above cited. The fact that in the contract plaintiff in error agreed that the Associated Oil Company would drill the well in question instead of agreeing to do so himself does not change the nature of the contract or make it a betting proposition, as plaintiff in error suggests. The object of the contract is the same whether plaintiff in error agreed personally to accomplish that object or to have the Associated Oil Company accomplish it for him. It is just the same from a legal standpoint.

Plaintiff in error also contends that the contract in suit provided for a penalty and not liquidated damages because the provision for the payment of the ten thousand dollars was in effect security for performance and not a sum to be paid in lieu of performance, citing 17 Corpus Juris, 933. It is quite apparent from reading the contract that if plaintiff in error did not perform said contract he was to pay the sum of ten thousand dollars as liquidated damages. Certainly this sum was to be paid

in lieu of performance. In arguing this point plaintiff in error states on page 13 of his brief:

> "That the guaranty executed by this defendant gave the Associated Oil Company no choice of anything in lieu of performance."

The obvious answer to this statement is that the contract was not with the Associated Oil Company. The Associated Oil Company owed no duty to defendant in error or defendant in error to Associated Oil Company as there was no privity of contract between them.

The remaining contention of plaintiff in error is that the contract in suit is a contract of guaranty, or in other words, a contract by which plaintiff in error

> "promised to answer for the debt, default or miscarriage of another person;"

that the Associated Oil Company was that other person and that plaintiff in error was discharged from any obligation under his contract of guaranty because the Midnight Oil Company and defendant in error failed to perform the provision of the contract, the performance of which was guaranteed, namely, the contract between the Midnight Oil Company and the Associated Oil Company relating to the drilling of the well in question. Plaintiff in error argues that by the terms of the said contract the Midnight Oil Company and defendant in error were obligated to deliver the possession of the

property in question to the Associated Oil Company; that the delivery of such possession was a condition precedent to the obligation of the Associated Oil Company to drill; that the failure to perform this condition precedent naturally released the Associated Oil Company from any obligation to perform and consequently released plaintiff in error from any and all obligations under his contract of guaranty. A careful examination of the documents attached to the answer of plaintiff in error and the instrument sued upon discloses the weakness of the foregoing argument. In the first place defendant in error was not a party to the contract, the performance of which by the Associated Oil Company, plaintiff in error claims he guaranteed. That contract is one solely between the Hopewell Oil Company and the Associated Oil Company. (Tr. page 19.) It is true, the Hopewell Oil Company assigned a portion of the benefits of its said contract with the Associated Oil Company to defendant in error (Tr. pages 26, 27, 28), but by the terms of the assignment defendant in error does not assume or agree to assume any of the obligations of the Hopewell Oil Company in its contract with the Associated Oil Company. It merely was to receive

> "the royalties and benefits accruing or hereafter accruing to the Hopewell Oil Company from the Associated Oil Company."

It is self-evident that an assignment by the Hopewell Oil Company of a portion of the royalties and

benefits which it expected to receive from its contract with the Associated Oil Company created no privity of contract between the Associated Oil Company and defendant in error. It follows therefore that defendant in error was under no legal obligation to perform any of the terms and conditions of the said contract on the part of the Hopewell Oil Company to be performed. This being true, it is difficult, if not impossible, to see how defendant in error by its failure to deliver the possession of the property to be drilled upon by the Associated Oil Company violated any duty either to the Associated Oil Company or to plaintiff in error. Surely it can not be successfully shown, so far as the record in this case is concerned, that there was any obligation on the part of defendant in error to dispossess those third parties whom plaintiff in error claims were holding the property in question adversely to defendant in error as well as to the Associated Oil Company. It is a well settled principle of law that the interference of a third party, unless provided for in the contract, is no excuse for the failure of a party to the contract to perform its terms and conditions on his part to be performed.

13 Corpus Juris 637;

6 R. C. L., pp. 1014, 1015;

Roberts v. Am. Col. & Lbr. Co. (W. Va.), 85 S. E. 535;

Stone v. Dennis, 3 Port. (Ala.) 231;

Gulf Ref. Co. v. Pegash Bros. (Texas), 146 S. W. 719.

If plaintiff in error had merely guaranteed that the Associated Oil Company would perform its said contract with the Hopewell Oil Company and the Hopewell Oil Company had prevented the Associated Oil Company from performing its said contract then it might well be argued that plaintiff in error would have been released of all obligations under his guaranty. But plaintiff in error did not guarantee that the Associated Oil Company would perform its contract with the Hopewell Oil Company. The agreement with plaintiff in error was that the Associated Oil Company would drill the oil-well in question commencing on or before the 15th day of June, 1919, and continue said drilling, barring unavoidable delays, until the oil well was completed. It is plain to be seen that this agreement was absolutely independent of any agreement which the Associated Oil Company had with the Hopewell Oil Company, and that it in no manner purports to guarantee the performance of that contract. It is a direct agreement by plaintiff in error that the Associated Oil Company would do a certain thing, namely, drill an oil-well. That contract was broken when the Associated Oil Company failed to drill said well. Defendant in error dismissed its suit against plaintiff in error in order to get this positive agreement from plaintiff in error. Defendant in error evidently desired to have some further assurance that the Associated Oil Company would drill the well other than the mere agreement of the Asso-

ciated Oil Company with the Hopewell Oil Company to do so in case the Hopewell Oil Company performed certain acts such as the delivery of the possession of the property in question.

Plaintiff in error claims that the trial court erred in overruling the demurrer to the complaint because the complaint does not allege

> "That the Associated Oil Company was not prevented by unavoidable delays from commencing to drill and thereafter to complete the well provided for in the contract."

In the first place there is no provision in the contract excusing a failure to commence drilling by the 15th day of June, 1919. The unavoidable delay portion of the contract refers to delays after drilling had once commenced. The reason for this distinction is quite apparent because the lease between the Hopewell Oil Company and The Western States Oil and Land Company provided for a forfeiture in case drilling operations were not commenced on or before the 15th day of June, 1919. However the above matter which plaintiff in error claims defendant in error should have alleged in its complaint is in its nature a matter of defense. It certainly would not be up to defendant in error to prove a negative or facts which are presumably within the sole knowledge of plaintiff in error or the Associated Oil Company.

Plaintiff in error also claims that the court erred in directing judgment to be entered in favor of

plaintiff and against defendant in accordance with the prayer of plaintiff's complaint, because the court should have required defendant in error to prove by evidence that it was impracticable or extremely difficult to fix actual damages and that defendant in error had suffered some damage as the result of the breach of contract by plaintiff in error. These points have been fully covered in the first portion of this brief to which reference is hereby made.

In conclusion, and by way of summary, defendant in error contends, as follows:

(1) That the contract between plaintiff and defendant in error was not a contract of guaranty, but a positive and independent agreement that the oil-well in question would be drilled in the manner specified; that no action taken by the Hopewell Oil Company or failure of the Hopewell Oil Company to act in relation to its contract with the Associated Oil Company in any manner affected the obligations existing between plaintiff in error and defendant in error.

(2) That there was no privity of contract between defendant in error and the Associated Oil Company, and that therefore defendant in error was under no legal duty to deliver possession of the property in question to the Associated Oil Company; that there was no agreement between plaintiff in error and defendant in error to the effect that defendant in error would deliver possession of the

property in question to the Associated Oil Company; that therefore plaintiff in error can not resort to such failure as a defense.

(3) That if some independent agency over whom defendant in error had no control, to-wit: third parties, claiming the real property in question adversely to defendant in error and others, interfered to prevent the Associated Oil Company from drilling the well in question it was no affair of defendant in error. Certainly such third parties were in no sense the agents of defendant in error and in absence of a contract to that effect it cannot be held legally for their acts; that so far as the parties to this action are concerned it was up to plaintiff in error to see that the Associated Oil Company was placed in possession of the property so as to enable it to drill. Of course it would be an entirely different matter if the answer alleged or in any manner showed that plaintiff in error had done anything to prevent the Associated Oil Company from commencing to drill or drilling the well in question, but the answer plainly alleges that the reason why the Associated Oil Company did not drill as agreed was because third parties claiming adversely to defendant in error prevented such drilling by refusing to permit the Associated Oil Company to go into possession of the property.

(4) That all that is required of a complaint seeking to recover liquidated damages is that it show that the nature of the case is such that it would be

impracticable or extremely difficult to fix actual damages; that when the contract sued upon itself does not show that it was a proper case for the parties to stipulate the damages, then the pleader may be required to allege and prove that it was impracticable and extremely difficult to fix the damages, but that no such requirement is made when the contract sued upon shows upon its face that it is impracticable and extremely difficult to fix the damages which would be occasioned by its breach; that the denial in the answer in the case at bar that it was impracticable to fix the actual damages is a denial which is refuted upon the very face of the complaint, thereby entitling defendant in error, so far as such denial is concerned, to judgment upon the pleadings.

(5) That in a contract where the parties have properly agreed upon liquidated damages the question of actual damages is eliminated and such question therefore becomes irrelevant in a suit based upon such contract.

For the foregoing reasons judgment of the trial court should be sustained.

Dated, San Francisco,
June 29, 1923.

Respectfully submitted,
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